

RESTRAINT OF TRADE AGREEMENTS IN EMPLOYMENT CONTRACTS: TIME FOR *PACTA SUNT SERVANDA* TO BOW OUT?

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1 Introduction

Despite the right to freedom of trade as provided for in section 22 of the Constitution of the Republic of South Africa, 1996, the maxim *pacta sunt servanda*, which has been regarded as more important than the value of freedom to trade since the judgment in *Magna Alloys v Ellis*¹ (“*Magna Alloys*”), is still given primacy in many court decisions. Several judgments after the advent of the Constitution merely confirmed the common law principles pertaining to agreements in restraint of trade and held that these were not in conflict with constitutional principles.² In *Magna Alloys* the Appellate Division held that a contract in restraint of trade is enforceable like any other contract freely entered into, unless it is against public policy.³ The position in South African law following this case was thus that, unless the covenantor (employee) could prove that the terms of the restraint are unreasonable and against public policy, the restraint would be enforceable. This is in contrast to the position in English law (which was followed by South African courts up to the *Magna Alloys* case) in terms of which a contract in restraint of trade is regarded as against public policy and thus unenforceable, unless the covenantee (employer) proves that it is not unreasonable.⁴

Against this background, Davis J of the Cape High Court held in *Advtech Resourcing Ltd t/a Communicate Personnel Group v Kuhn*⁵ (“*Advtech*”) that the common law contract is now subject to constitutional rights and that the employer should thus bear the onus of proving that a contract in restraint of trade is reasonable.⁶

Later in 2008 the Durban High Court came to a completely opposite conclusion in *Den Braven Ltd v Pillay*⁷ (“*Den Braven*”). Wallis J held that section 22 has no direct application to contracts in restraint of trade, that *Advtech* was wrongly decided and that the enforceability of contracts in

¹ 1984 4 SA 874 (A)

² *Walton's Stationery Co (Edms) Bpk v Fourie* 1994 4 SA 507 (O) 513; *Knox D'Arcy v Shaw* 1996 2 SA 651 (W) 661; *Oasis Group Holdings (Pty) Ltd v Bray* 2006 4 All SA 183 (C) para 30

³ *Magna Alloys v Ellis* 1984 4 SA 874 (A) 893

⁴ *Mason v Provident Clothing and Supply Company Limited* [1913] AC 724 733
⁵ 2008 2 SA 375 (C)

⁶ *Advtech Resourcing Ltd t/a Communicate Personnel Group v Kuhn* 2008 2 SA 375 (C) para 28

⁷ 2008 6 SA 229 (D)

restraint of trade should still be interpreted in terms of the principles laid down in *Magna Alloys*.⁸

This article will deal with these conflicting interpretations of the impact of the Constitution on agreements in restraint of trade as part of employment contracts. These opposing views call for the issue to be resolved by either the judiciary or legislator in the interests of clarity and certainty. There is support for both interpretations in cases decided before and after these judgments as will be discussed below. The need for a fundamental reconsideration of which principle should enjoy preference, namely *pacta sunt servanda* or freedom to trade in establishing public policy, as well as the connected issue of who should bear the onus, will be discussed.

2 The detrimental impact of *Magna Alloys* on employees

The English position that contracts in restraint of trade are against public policy and therefore *prima facie* void,⁹ was followed by South African courts, apparently without any analysis of whether there existed any basis for such a rule in the South African common law.¹⁰ In *Magna Alloys* the Appellate Division held that there was no rule in Roman-Dutch law to the effect that contracts in restraint of trade were unenforceable.¹¹ The court's decision is based on only two texts in regard to, firstly, an agreement between partners not to compete after dissolution of the partnership, and secondly, an agreement not to compete after the sale of a business. From these texts it is clear that the agreements were not regarded as *prima facie* invalid and that they were enforced by the Hooft Raad.¹² Although these two cases do not concern restraint agreements in respect of employment contracts, the court in *Magna Alloys* clearly did not regard this as significant. The court also did not take the legal position on monopolies into consideration. In several texts it is clearly stated that monopolies infringing the freedom of trade in Roman-Dutch law were regarded as harmful.¹³ Restraints which were prejudicial to the public in this context were invalidated by the courts.¹⁴

The court in *Magna Alloys* accepted that the restraint agreements against the public interest will not be enforceable and that an unreasonable restraint (in regard to the interest to be protected) will usually be against the public interest.¹⁵ The court stated that it is in the public interest that persons honour their own agreements. The fact that an agreement is unreasonable or unfair

⁸ Para 35

⁹ *Nordenfelt v The Maxim Nordenfelt Guns and Ammunition Co Ltd* [1894] AC

¹⁰ *Holmes v Goodall and Williams* 1936 CPD 35 42; *Super Safes (Pty) Ltd v Voulgarides* 1975 2 SA 783 (W) 785D-F

¹¹ *Magna Alloys v Ellis* 1984 4 SA 874 (A) 890

¹² 890

¹³ JT Schoombee "Agreements in Restraint of Trade: The Appellate Division confirms New Principles" (1985) 48 *THRHR* 127 135

¹⁴ Even in Roman times the principal task of the provincial governor was to protect freedom of professional activity (A Wacke "Freedom of Trade and Clauses in Restraint of Trade in Roman and Modern Law" (1993) 11 *Law and History Review* 1 4) Restraint of trades in the employment context arose in regard to a freed slave and his master Roman law did not allow the master to place a restraint on competition of his former slave (Wacke (1993) *Law and History Review* 9)

¹⁵ *Magna Alloys v Ellis* 1984 4 SA 874 (A) 893

in regard to one of the parties will normally not provide any ground for challenging the validity of the agreement.¹⁶

The implication of the view that contracts in restraint of trade are *prima facie* enforceable is that the onus to prove that the agreement is unreasonable would henceforth in South African law (in contrast to English law) rest on the contracting party that wants to escape the clause. The court in *Magna Alloys* further held that, in contrast to English law, South African courts should take the time of enforcement of the contract as the relevant time for deciding whether enforcement would be in the public interest and therefore whether the restraint is reasonable. According to the court, it is logical and realistic that the court should be in a position to order that only part of the restraint should be enforced, if the court is to look at the circumstances at the time when enforcement is sought.¹⁷

The radical turnabout in *Magna Alloys* on established aspects of the restraint of trade law may be seen as part of the movement by South African courts to “purify” the South African legal system of English influences and to return to its Roman-Dutch roots.¹⁸ The implication of the judgment was that employees who were party to a restraint agreement were now in a weaker position than previously. The rules fundamental to the English doctrine were formulated to accommodate the unequal bargaining position of employees.¹⁹ This dimension was lost with the changing of the rules in *Magna Alloys*,²⁰ as the court did not distinguish between restraint clauses in general and those which are ancillary to employment contracts.

Other detrimental effects on employees²¹ were that the burden of proof that the restraint was unreasonable was now on the employee because of the primary position given to *pacta sunt servanda*. The court could also enforce that part of an overbroad restraint which is not detrimental to the public interest, in contrast to the position before *Magna Alloys*, when the strict “blue pencil” test²² was applied to severability of a restraint agreement. A further disadvantage was that the public interest was now the touchstone of reasonableness²³ and that reasonableness *inter partes* would no longer be the main factor for the enforceability of a restraint.

3 The development of the test for reasonableness after *Magna Alloys*

The court in *Magna Alloys* did not give guidelines on how reasonableness is to be established and, as indicated above, placed emphasis on the public

¹⁶ 893

¹⁷ 896

¹⁸ E Fagan “Roman-Dutch Law in its South African Historical Context” in R Zimmermann & D Visser (eds) *Southern Cross: Civil Law and Common Law in South Africa* (1996) 33 60–64

¹⁹ *Nordenfeldt v The Maxim Nordenfeldt Guns* 1894 A C 535 566:

“[T]here is obviously more freedom of contract between buyer and seller than between master and servant or between an employer and a person seeking employment”

²⁰ Schoombee (1985) *THRHR* 140

²¹ 134

²² 148

²³ *Magna Alloys v Ellis* 1984 4 SA 874 (A) 892

interest and not on reasonableness *inter partes*. The test for reasonableness was developed in the following way in *Sunshine Records v Frohling*:²⁴

“[I]t is detrimental to society if an unreasonable fetter is placed on the person’s freedom to trade or to pursue a profession and that would in general be contrary to the public interest to enforce an unreasonable restriction on a person’s freedom to trade.”²⁵

In *Basson v Chilwan*²⁶ the court held that the following factors should be taken into account in deciding whether a restraint of trade is reasonable and consequently enforceable:

1. Is there an interest of the one party which is deserving of protection after termination of the agreement?
2. Is such interest being prejudiced by the other party?
3. If so, does such interest weigh qualitatively and quantitatively against the interest of the other party that the latter should not be economically inactive and unproductive?
4. Is there any other facet of public policy having nothing to do with the relationship between the parties but which requires that the restraint should either be maintained or rejected?²⁷

This proportionality test, in which the interests of the employer and employee are balanced, has been followed by most courts in the post-*Magna Alloys* era. Courts have held that the restraint would be unreasonable if its only purpose is to eliminate competition.²⁸ The employer must possess a protectable interest, which may include confidential information, trade secrets or trade connections.²⁹ If the geographical area is too wide, or if the time during which the restraint would operate is too long, the restraint will be regarded as unreasonable.³⁰ The focus is clearly on the interests of the employer and factors that could have an impact on the interests of the employee have seldom been taken into consideration.

4 Conflicting judgments on the impact of section 22

The principles laid down in *Magna Alloys* were followed by South African courts for close to two decades. The protection of freedom to trade in the Constitution raised questions about whether these principles were in conflict with the Constitution. Section 26 of the interim Constitution protects the right

²⁴ 1990 4 SA 782 (A)

²⁵ 794C-E

²⁶ 1993 3 SA 742 (A) 767

²⁷ “The use of gifts and bribes by the applicant to woo or maintain customers” was regarded as such a factor in *Arrow Altech Distribution v Byrne* 2008 29 ILJ 1391 (D) 1409 para 76

²⁸ *Basson v Chilwan* 1993 3 SA 742 (A) 763; *Sibex Engineering v Van Wyk* 1991 4 SA 482 (T) 508

²⁹ *Recycling Industries (Pty) Ltd v Mohammed* 1981 3 SA 250 (SE) 258G-H; *Basson v Chilwan* 1993 3 SA 742 (A) 769H; *Sibex Engineering Services (Pty) Ltd v Van Wyk* 1991 4 SA 482 (T) 509

³⁰ *Sibex Engineering Services (Pty) Ltd v Van Wyk* 1991 4 SA 482 (T) 511

to freely *engage* in economic activity³¹ and section 22 of the final Constitution provides that every citizen has the right to *choose* their trade, occupation or profession freely³² (emphasis added).

Although section 22 of the final Constitution may be regarded as more limited³³ than section 26 of the interim Constitution, Sutherland rightly argues that the most important aspect of freedom of trade is the freedom to work.³⁴ It is clear that the right to choose a trade, occupation or profession also includes the right to practise the trade, occupation or profession. If not, the right to choose would be meaningless.

Several cases decided after the advent of the Constitution held that the Constitution had no influence on the common law as set out in *Magna Alloys*. In *Knox D'Arcy v Shaw*³⁵ Van Schalkwyk J justified this view as follows:

"The Constitution does not take such a meddlesome interest in the private affairs of individuals that it would seek, as a matter of policy, to protect them against their own foolhardy or rash decisions ... The provenance of the English rule that a contract in restraint of trade is *prima facie* unlawful refers back to a time when employees were inherently disadvantaged when striking a bargain with their employers ... it is evident that the principle underlying English law has long since been overtaken by events and that there are now no reasons of public policy why an employee who voluntarily undertakes a restraint should be presumed to be at a disadvantage".³⁶

This view of a "passive" role of the Constitution reflects a philosophy of non-interference of public law with private contractual relationships and a disregard for the inequality of bargaining position of the employee which was prevalent in legal thinking when *Magna Alloys* was decided.³⁷ The above reasoning that the Constitution had not altered the *status quo* and that restraint agreements in employment contracts should not be treated differently to other types of contracts was recently followed by Wallis J in *Den Braven v Pillay*.³⁸ The argument in these cases that employees are no longer in a disadvantaged position when contracting with the employer is not substantiated in any of these cases.

In contrast to the above cases, the influence of the Constitution on restraint agreements was acknowledged in several cases. In *Coetsee v Comitiss*,³⁹

³¹ S 26 of the Constitution of the Republic of South Africa Act 200 of 1993 provides that:

"(1) Every person shall have the right freely to engage in economic activity and to pursue a livelihood anywhere in the national territory
(2) Subsection (1) shall not preclude measures designed to promote the protection or improvement of the quality of life, economic growth, human development, social justice, basic conditions of employment, fair labour practices or equal opportunity for all, provided such measures are justifiable in an open and democratic society based on freedom and equality"

³² S 22 of the final Constitution provides that:

"Every citizen has the right to choose their trade, occupation or profession freely. The practice of a trade, occupation or profession may be regulated by law"

³³ D Davis "Freedom of Trade, Occupation and Profession" in S Woolman, T Roux & M Bishop (eds) *Constitutional Law of South Africa* 2 ed (RS 2009 1) 54-1

³⁴ PJ Sutherland *The Restraint of Trade Doctrine in England, Scotland and South Africa* PhD thesis Edinburgh (1997) 31

³⁵ 1996 2 SA 651 (W)

³⁶ 659

³⁷ Davis J refers to this approach as a libertarian view of the world in *Advtech Resourcing (Pty) Ltd v Kuhn* 2008 2 SA 375 (C) para 31

³⁸ *Den Braven Ltd v Pillay* 2008 6 SA 229 (D) para 27

³⁹ 2001 1 All SA 538 (C)

Traverso J considered the impact of the Constitution on public policy as follows:

“[C]onsiderations of public policy cannot be constant. Our society is an ever-changing one. We have moved from a very dark past into a democracy where the Constitution is the supreme law, and public policy should be considered against the background of the Constitution and the Bill of Rights. One can think of many situations which would, prior to 1994, have been found not to offend public policy which would today be regarded as inhuman.”⁴⁰

Traverso J held that the rules of the National Soccer League (“NSL”), which formed part of the contracts of soccer players, infringed the following rights of the players: freedom of movement, the right to choose a profession or occupation freely and the right to dignity. The court stated that the players were treated as “goods and chattels”⁴¹ in terms of a contract akin to a restraint of trade and that they had no freedom of contract. As the restraint infringed the constitutional rights of players, “the onus lies with the NSL to satisfy this Court that the compensation regime [part of the restraint contract] is a reasonable and justifiable limitation in an open and democratic society based on human dignity, equality and freedom, taking into account all relevant factors.”⁴²

The court in *Coetzee v Comitis* therefore found that the specific contract offended public policy as informed by the Constitution and also infringed specific constitutional rights of players. The party that wished to enforce the contract had to bear the onus of proving that it is a justifiable limitation in terms of section 36 of the Constitution.

In several cases decided after *Coetzee v Comitis*, the courts agreed with Traverso’s approach. In *Lifeguards Africa v Raubenheimer*,⁴³ Tshabalala JP held that the onus should be on the employer where the constitutional right to freedom of trade of the employee is limited, but considered the court bound to *Magna Alloys and Bridgestone, Firestone, Maxipriest Ltd v Taylor*.⁴⁴ In *Canoa KwaZulu-Natal v Booth*⁴⁵ the Natal High Court also held that it is inconsistent with the Constitution to impose the onus to prove a constitutional protection on the employee.⁴⁶ In *Fidelity Guard Holdings (Pty) Ltd t/a Fidelity Guards v Pearmain*,⁴⁷ Liebenberg J stated that

“it seems that the position in terms of the Constitution may now be that the onus will be on the party wishing to enforce it to show that it complies with the provisions of the Constitution.”⁴⁸

⁴⁰ Para 31

⁴¹ Para 38

⁴² Para 40

⁴³ 2006 5 SA 364 (D&CLD)

⁴⁴ 2003 1 All SA 299 (N)

⁴⁵ 2004 1 BCLR 39 (N)

⁴⁶ However, in *Rectron (Pty) Ltd v Govender* 2006 CLR 1 (D) the court found that the judgment in *Canoa* was clearly wrong on the ground that Kondile J had not considered the judgments delivered by the High Court in which it was held that the Constitution had no impact on the onus in restraint of trade agreement. No analysis of the meaning of s 22 was made. The court in *Rectron* accordingly adhered to the principles laid down in *Magna Alloys*.

⁴⁷ 2001 2 SA 853 (SE)

⁴⁸ 862F-H

Unfortunately the judge did not go further than this and did not make a decision on the matter as it was not necessary for the purposes of the specific judgment.

In *Oasis Group Holdings (Pty) Ltd v Bray*⁴⁹ the Cape High Court acknowledged that the court in two judgments, namely *Coetzee v Comitis*⁵⁰ and *Canoa KwaZulu-Natal (Pty) Ltd t/a Canon Office Automation v Booth*,⁵¹ held that section 22 of the Constitution had the effect that the onus of proving that a restraint should be enforced has now shifted to the employer. However, Dlodlo J considered the court to be bound to *Magna Alloys*.⁵²

The above discussion indicates that there was disagreement in regard to whether the Constitution has an impact on the common law rule of the primacy of sanctity of contract as established by *Magna Alloys* and the concomitant rule that the employee bears the onus in restraint contracts. In some instances the High Court considered it bound to *Magna Alloys* by the rules of *stare decisis* and did not consider the possibility that the court could develop the common law rules which do not reflect constitutional values.⁵³ There was clearly a need for guidance from the Supreme Court of Appeal or the Constitutional Court.⁵⁴

5 A golden opportunity missed in *Reddy v Siemens*

In *Reddy v Siemens*⁵⁵ the SCA left open the question of the influence of section 22 on trade restraints. The court held that the onus issue would not have a bearing on the judgment, as all the evidence was before the court. What was called for was a value judgment:

“A court must make a value judgment with two principal policy considerations in mind in determining the reasonableness of a restraint. The first is that the public interest requires that parties should comply with their contractual obligations, a notion expressed by the maxim *pacta servanda sunt*. The second is that all persons should in the interests of society be productive and be permitted to engage in trade and commerce or the professions. Both considerations reflect not only common-law but also constitutional values. Contractual autonomy is part of freedom informing the constitutional value of dignity, and it is by entering into contracts that an individual takes part in economic life. In this sense freedom to contract is an integral part of the fundamental right referred to in s 22. Section 22 of the Constitution guarantees ‘[e]very citizen ... the right to choose their trade, occupation or profession freely’ reflecting the closeness of the relationship between the freedom to choose a vocation and the nature of a society based on human dignity as contemplated by the Constitution. It is also an incident of the right to property to the extent that s 25 protects the acquisition, use, enjoyment and exploitation of property, and of the fundamental rights in respect of freedom of association (s 18), labour relations (s 23) and cultural, religious and linguistic communities (s 31).”⁵⁶

⁴⁹ 2006 4 All SA 183 (C)

⁵⁰ 2001 1 All SA 538 (C)

⁵¹ 2004 1 BCLR 39 (N)

⁵² *Oasis Group Holdings (Pty) Ltd v Bray* 2006 4 All SA 183 (C) 195

⁵³ See the exposition of Brand AJ in *Afrox Healthcare v Strydom* 2002 4 All SA 125 (SCA) paras 27-30. The judge explains that if the High Court is convinced that a rule of the common law is in conflict with the Constitution, the court is obliged to deviate from the common law rule. However, if there is no direct conflict between the common law rule and the Constitution, the High Court is bound to the rules of *stare decisis*.

⁵⁴ For a discussion of the tension between the principle of *stare decisis* and s 39(2) of the Constitution see MA du Plessis “*Stare Decisis: Is the Onus in Restraint of Trade hanging on a Thread?*” (2006) *TSAR* 423

⁵⁵ (2007) 28 ILJ 317 (SCA)

⁵⁶ Para 15

In spite of acknowledging the influence of the Constitution in the above paragraph and the balancing of the principles of *pacta sunt servanda* and freedom of trade, the court in *Reddy* added:

“Where the onus lies in a particular case is a consequence of the substantive law on the issue. I have pointed out that the substantive law in *Magna Alloys* is that a restraint is enforceable unless it is shown to be unreasonable, which necessarily casts an onus on the person who seeks to escape it.”⁵⁷

The Supreme Court of Appeal was clearly reluctant to find that the South African trade restraint law had been changed by constitutional principles and preferred *pacta sunt servanda* as the primary value with the effect that the onus remains on the employee.

Neethling⁵⁸ states that Malan J neatly avoided the question of onus by stating that since all the evidence was before the court, the incidence of the onus would not make a difference. Neethling himself also avoids the question by stating the following:

“It is submitted that this approach should be followed in similar circumstances in future, thus steering clear of the rather intricate question of whether the substantive law governing the burden of proof should be changed.”⁵⁹

Why should courts steer away from this question? There is an urgent need for certainty, as indicated above. In an endeavour to answer the above question, the nature of *pacta sunt servanda* and freedom to trade will be analysed below.

The decision in *Reddy* was followed in *Arrow Altech Distribution (Pty) Ltd v Byrne*.⁶⁰ In this case Nicholson J summarised restraint of trade law and stated that

“where the onus lies in a particular case is a consequence of the substantive law on the issue. What that calls for is a value judgment, rather than a determination of what facts have been proved, and the incidence of the onus accordingly plays no role.”⁶¹

Nicholson J apparently understood that *Reddy* held that the onus does not play a role any longer, while *Reddy* only held that it did not play a role in the particular case and, in fact, endorsed the view that the employee should bear the onus.

In *Dickinson Holdings v Du Plessis*⁶² (also following *Reddy*) it was accepted that the person who wants to escape the restraint clause in a contract had to prove that it was unreasonable and by implication that the Constitution had no influence on the onus.⁶³ It is against this background of uncertainty about the constitutional impact on restraint agreements that the conflicting judgments of Davis J in *Advtech v Kuhn*⁶⁴ and Wallis J in *Den Braven v Pillay*⁶⁵ were

⁵⁷ Para 14

⁵⁸ J Neethling “The Constitutional Impact on the Burden of Proof in Restraint of Trade Covenants – A Need for Exercising Restraint” (2008) 20 *SA Merc LJ* 89 94

⁵⁹ 94

⁶⁰ 2008 29 *ILJ* 1391

⁶¹ Para 4

⁶² 2008 *ILJ* 1666

⁶³ Para 89

⁶⁴ 2008 2 SA 375 (C)

⁶⁵ 2008 6 SA 229 (D)

handed down. Davis J gave priority to the principle of freedom of trade and Wallis J gave priority to sanctity of contract.

6 The result of the unresolved disagreement: the battle of the judges

Davis J held in *Advtech v Kuhn* that the importance ascribed to the dignity of work⁶⁶ supports the view that the onus should be on the employer to prove that the restraint is not unreasonable.⁶⁷ The judge in effect held that the primary position of *pacta sunt servanda* in restraint agreements should now be occupied by the right to work, which is protected in section 22 of the Constitution.

The court in *Advtech* relied on the judgment of the Constitutional Court in *Barkhuizen v Napier*⁶⁸ (“*Barkhuizen*”) to emphasise that in the post-constitutional era contracts are subject to the Constitution.⁶⁹ In *Barkhuizen* Ngcobo J emphasised the importance of *pacta sunt servanda*, but cautioned that contracts which are against public policy would never be enforced⁷⁰ and that public policy in South Africa is now informed by the Constitution. Every contract may be examined to ensure that it is not against public policy. The court in *Barkhuizen* further stated that there are constitutional values embodied in the principle of contractual autonomy, namely the right to regulate one’s own life, which forms part of the constitutional rights to dignity and equality.⁷¹ However, the judge cautioned that unequal bargaining relationships may have the implication that there is no contractual autonomy and had the insured in this case brought any evidence that he was in an unequal bargaining position, the court would have taken this into account.⁷² The judgment in *Barkhuizen* was criticised for not directly applying section 34 of the Constitution (the right to access to the courts) to the insurance contract in this case, but for using public policy, as informed by the Constitution, as a yardstick.⁷³

In *Den Braven v Pillay*⁷⁴ Wallis J emphasised that *pacta sunt servanda* is the economic life-blood of a civilised country and that the primacy of this principle as set out in *Magna Alloys* is still binding. The judge criticised Davis J’s statement in *Advtech v Kuhn* that adherence to *pacta sunt servanda* is an indication of a libertarian view of contractual relations.⁷⁵ It is clear that Wallis J did not agree with the tenet of Davis J’s argument that adherence to *pacta sunt servanda* (without taking the influence of power relationships on consensus into account) is a reflection of the old view of *laissez faire* which previously allowed for complete freedom of contract, unless specifically regulated by statute. Wallis J held that there is no need to treat contracts in

⁶⁶ See *Affordable Medicines Trust v Minister of Health* 2006 3 SA 247 (CC) para 59

⁶⁷ *Advtech Resourcing Ltd t/a Communicate Personnel Group v Kuhn* 2008 2 SA 375 (C) para 28

⁶⁸ 2007 7 BCLR 691 (CC)

⁶⁹ Para 11

⁷⁰ Para 15

⁷¹ Para 57

⁷² Para 66

⁷³ S Woolman “The Amazing, Vanishing Bill of Rights” (2007) 4 *SALJ* 762 772

⁷⁴ 2008 6 SA 229 (D)

⁷⁵ Para 31

restraint of trade differently to any other contract as “problems that may arise from the disparate power relationships of the parties are dealt with in a variety of ways and particularly by legislation”.⁷⁶ This view reflects the philosophical foundations of the judgments in *Roffey v Catterall*, *Edwards & Goudré*,⁷⁷ *Magna Alloys v Ellis*⁷⁸ and *Knox D’Arcy v Shaw*,⁷⁹ a case decided under the interim Constitution, but which adhered to the views of pre-constitutional cases. At this point it must be noted that there is no existing South African legislation protecting employees at the conclusion of a restraint in trade. This aspect will be discussed below.

Wallis J held that section 22 of the Constitution has no direct influence on restraint of trades as it does not have horizontal working.⁸⁰ The judge based his argument on the second part of section 22, which provides that “the practice of a trade, occupation or profession may be regulated by law”. He argued that this phrase indicates that the section only has vertical working. In the light of section 8 of the Constitution, this argument cannot be accepted, as there is nothing in the first part of the section that indicates that it should not be applicable to private parties. Furthermore, in *Brisley v Drotosky*⁸¹ the court had to decide whether section 26 of the final Constitution, which provides that no one may be evicted from their home, only had vertical working and came to the conclusion that although certain parts of the section are only applicable to the state, this is no reason why other parts of the section should not also be applicable to private parties.⁸²

From the above and from cases decided after the *Advtech* and *Den Braven* cases, it is clear that there is a lack of certainty about whether the Constitution does have an influence on the common law principles applicable to restraints of trade and, if so, the extent of its influence.⁸³ Guidance is needed on the question of whether *pacta sunt servanda* is still the primary value or whether it has now been replaced by the right to freedom to trade and, if so, how the common law should be developed to reflect constitutional values.

7 Two routes for developing the common law to give effect to section 22

In *Khumalo v Holomisa*⁸⁴ the Constitutional Court held that section 8 of the Constitution does have horizontal application and that it is therefore

⁷⁶ Para 33

⁷⁷ 1977 4 SA 494 (N)

⁷⁸ 1984 4 SA 874 (A)

⁷⁹ 1996 2 SA 651 (W)

⁸⁰ Rautenbach labels this approach “a deconstitutionalising of constitutional rights” IM Rautenbach “Constitution and Contract – Exploring the Possibility that Certain Rights may apply directly to Contractual Terms or the Common Law that underlies Them” (2009) *TSAR* 613 625

⁸¹ 2002 12 BCLR 1229 (SCA)

⁸² *Brisley v Drotosky* 2002 12 BCLR 1229 (SCA) paras 39-42

⁸³ In *Random Logic (Pty) Ltd t/a Nashua Cape Town v Dempster* 2009 30 *ILJ* 1762 (C) para 31, Bozalek J stated that

“whether the employee’s s 22 right will play a more decisive role in the evaluation of the reasonableness of restraint of trade agreements through the direct route envisaged by Davis J in *Advtech* or through the vehicle of public policy remains to be seen”

⁸⁴ 2002 8 BCLR 771

applicable to a dispute between private parties. In that case the Constitutional Court applied a provision of the Bill of Rights (freedom of expression) to the common law rule of defamation. The court held that if the common law of defamation did not give effect to the right to freedom of speech, the common law should be developed in terms of section 8(3) of the Constitution⁸⁵ to give effect to the constitutional right.

However, in *Barkhuizen v Napier* Ngcobo J for the majority held that it was inappropriate to test a contractual clause against a constitutional right in terms of section 8. Direct application of a constitutional right to a contract was the route followed by the High Court in the same case. Ngcobo J criticised this mode of establishing whether there had been an infringement of a constitutional right and reasoned that the correct way of testing the constitutionality of a contractual clause is to establish whether the clause “goes against” the values embodied in the Constitution and then to develop the common law rules in line with section 39(2) of the Constitution.⁸⁶

“In my view the proper approach to the constitutional challenges to contractual terms is to determine whether the term challenged is contrary to public policy as evidenced by the constitutional values, in particular those found in the Bill of Rights. This approach leaves space for the doctrine of *Pacta sunt servanda* to operate, but at the same time allows courts to decline to enforce contractual terms that are in conflict with the constitutional values even though the parties may have consented to them.”⁸⁷

In his concurring judgment, Langa CJ was not convinced that section 8 does not allow for the possibility that certain rights may apply directly to contractual terms. The above approach of Ngcobo J is also criticised by Woolman, who argues that this way of reasoning is a conflation of values, rights and public policy analysis.⁸⁸ Sutherland is equally critical of the Constitutional Court’s approach and states that phrases used by Ngcobo J such as “constitutional values particularly those found in the Bill of Rights” are confusing and disrespectful of the Constitution and that this “demotes specific rights to the level of values.”⁸⁹ Rautenbach views the reluctance of courts to apply constitutional rights directly to the law that underlies contractual terms as a resistance of private law individual autonomy to the influence of constitutional human rights.⁹⁰

However, there is merit in the Constitutional Court’s criticism of the approach of the High Court which heard the matter in the first instance, with regard to the direct application of constitutional rights to the terms of a specific

⁸⁵ S 8(3) of the Constitution provides:

“When applying a provision of the Bill of Rights to a natural or juristic person in terms of subsection (2), a court—

(a) in order to give effect to a right in the Bill, must apply, or if necessary develop, the common law to the extent that legislation does not give effect to that right; and
(b) may develop rules of the common law to limit the right, provided that the limitation is in accordance with section 36 (1)”

⁸⁶ S 39(2) of the Constitution provides:

“When interpreting any legislation, and when developing the common law or customary law, every court, tribunal or forum must promote the spirit, purport and objects of the Bill of Rights”

⁸⁷ *Barkhuizen v Napier* 2007 7 BCLR 691 (CC) para 30

⁸⁸ Woolman (2007) *SALJ* 772

⁸⁹ PJ Sutherland “Ensuring Contractual Fairness in Consumer Contracts after *Barkhuizen v Napier* I” (2008) 19 *Stell LR* 390 402

⁹⁰ Rautenbach (2009) *TSAR* 617

contract in terms of section 8.⁹¹ This approach of the High Court leads to difficulties, as a limitation of a constitutional right could only be justified in terms of section 36 of the Constitution, which provides that a right in the Constitution can only be limited by a law of general application. The terms of a specific contract cannot be regarded as “a law of general application”. The approach should be to test the law of contract, namely *pacta sunt servanda*, the common law rule in terms of which contracts are enforced, against the relevant constitutional right or rights.⁹² A common law rule could be seen as “a law of general application”. If this approach is applied to restraint of trade agreements, the common law rules of *pacta sunt servanda* particularly as applicable to restraint agreements (the test for reasonableness) should be tested against section 22 and other relevant constitutional rights.

Relying on the judgment in *Holomisa*, Davis J in *Advtech v Kuhn* argued that if it is found that the common law rule that the employee bears the onus in restraint of trade disputes limits constitutional rights impacting on the dignity to work, the common law should be developed in terms of section 8(3) of the Constitution to place the onus on the employer to prove that the limitation is constitutional.⁹³ This approach of Davis J has considerable merit in that section 8(3)(a) of the Constitution provides that a court “in order to give effect to a right in the Bill, must apply, or if necessary develop, the common law to the extent that legislation does not give effect to that right”. Since restraint of trade clauses in employment contracts have not been regulated by legislation (unlike most other areas of labour law), it is submitted that it is necessary that the courts develop this area of labour law to give effect to constitutional values.

This argument could be strengthened by taking into consideration certain judgments in which the common law contract of employment was developed in such a manner to be deemed to contain an implied right to fairness. This line of cases started with *Old Mutual v Gumbi*,⁹⁴ which was then followed *inter alia* by *Boxer Superstores Mthatha v Mbenya*,⁹⁵ before culminating in *Murray v Minister of Defence*.⁹⁶ In the latter case the court stated that

“the common law of employment must be held to impose on all employers a duty of fair dealing at all times with their employees.”⁹⁷

However, in *SA Maritime Safety Authority v McKenzie*⁹⁸ the SCA held that where an employee is covered by the Labour Relations Act, there is no implied right of fair labour practices in such a person’s contract of employment. Despite this judgment, it could be argued that *Murray* is still good law in regard to persons or aspects of the employment relationship not covered by the LRA

⁹¹ *Barkhuizen v Napier* 2007 7 BCLR 691 (CC)

⁹² Sutherland (2008) *Stell LR* 399

⁹³ *Advtech Resourcing Ltd t/a Communicate Personnel Group v Kuhn* 2008 2 SA 375 (C) para 28

⁹⁴ 2007 8 BLLR 699 (SCA)

⁹⁵ 2007 8 BLLR 693 (SCA)

⁹⁶ 2008 6 BLLR 513 (SCA)

⁹⁷ Para 5

⁹⁸ 2010 5 BLLR 488 (SCA)

and that since employment restraints are not covered by labour legislation, these contracts contain an implied right to fair dealing.

In the *Advtech* decision, Davis J further argued that the common law could, alternatively (to development in terms of section 8(3)(a) of the Constitution), be developed in terms of section 39(2) of the Constitution (as was done in *Barkhuizen v Napier*), which mandates courts to develop the common law to reflect the spirit, purport and objects of the Constitution.⁹⁹ For a development of the law in terms of section 39(2), there is no need for a direct conflict between the common law rule and the constitutional right.

The approach of Traverso J in *Coetzee v Comitis* and that of Davis J in *Advtech v Kuhn*, in terms of which the Constitution is applied directly¹⁰⁰ to a common law rule of contract, is to be preferred, as it acknowledges that entrenched rights are concretised rules of public policy. These rights should be enforceable and should not be dependent on a process of developing the common law to give effect to the spirit, purport and objects of the Constitution.

8 The demise of *pacta sunt servanda*

Courts in the pre-constitutional era held *pacta sunt servanda* in high regard as a profoundly moral principle and regarded sanctity of contract as more important than freedom to trade.¹⁰¹ This may be seen as a *laissez faire* approach according to which the most powerful party to the contract will get the best deal, as opposed to social intervention in terms of which the weaker party will be protected.¹⁰² In judgments on contracts in restraint of trade under the Constitution, several judgments held that sanctity of contract still holds primary place when weighed against freedom of trade in establishing the content of public policy.¹⁰³

Ncgobo J in *Barkhuizen v Napier* described the inappropriateness of primacy of sanctity of contract in a post-constitutional era as follows:

“The doctrine of sanctity of contract and the maxim *pacta sunt servanda* have through judicial and text-book repetition come to appear axiomatic, indeed mesmeric, to many in the legal world. Their virtue if applied in an unlimited way is not self-evident and their reach if not their essence have come to be severely restricted in open and democratic societies ... The jurisprudential pedestal on which it once imperiously stood has been singularly narrowed in the great majority of democratic societies. Our new constitutional order, I believe, further attenuates its one-time implacable application.”¹⁰⁴

However, in several judgments (including *Barkhuizen v Napier*) handed down after the advent of the Constitution, *pacta sunt servanda* has been read into the right to freedom and dignity.¹⁰⁵ The approach is that an individual's contractual autonomy is part of the constitutional right to dignity.¹⁰⁶ This

⁹⁹ *Advtech Resourcing Ltd t/a Communicate Personnel Group v Kuhn* 2008 2 SA 375 (C) paras 23-25

¹⁰⁰ These cases also made provision that the common law could be developed in terms of s 39(2) of the Constitution

¹⁰¹ *Roffey v Catterall, Edwards and Goudré (Pty) Ltd* 1977 4 All SA 482 (N) 493

¹⁰² B du Plessis & DM Davis “Restraint of Trade and Public Policy” (1984) 86 SALJ 86 97

¹⁰³ *Knox D'Arcy v Shaw* 1996 2 SA 651 (W) 661; *Reddy v Siemens* 2007 2 SA 486 (SCA) para 14.

¹⁰⁴ *Barkhuizen v Napier* 2007 7 BCLR 691 (CC) para 141

¹⁰⁵ *Barkhuizen v Napier* 2007 7 BCLR 691 (CC) para 57; *Brisley v Drotzky* 2002 12 BCLR 1229 (SCA) para 7; *Reddy v Siemens* 2007 2 SA 486 (SCA) para 15

¹⁰⁶ *Barkhuizen v Napier* 2007 7 BCLR 691 (CC) paras 30, 57

approach elevates *pacta sunt servanda* to a constitutional right which can be balanced against other constitutionally protected rights while there is no explicit reference to contractual autonomy in the Bill of Rights.¹⁰⁷ A deeper dimension of sanctity of contract in the restraint of trade context is that it protects the vested proprietary and commercial interests of the employer.¹⁰⁸

Sachs J in *Barkhuizen v Napier* illustrated that it is particularly inappropriate to rely on sanctity of contract where standard form contracts are used. The judge argues that these documents cannot be seen as consensual and that it is surprising that courts in modern times have enforced “contracts” of this kind in the light of the importance of the element of consent in the classic contract law.¹⁰⁹

9 The value protected by freedom to work

Section 22 of the Constitution provides that every citizen has the right to choose a trade, occupation or profession. The essence of this right is the freedom to earn a living by working. Sutherland points out that by using this terminology, the emphasis is placed where it should be, namely on the freedom to work.¹¹⁰

In the United Kingdom courts have often emphasised the high regard in that country for the liberty of a man to earn his living and the fact that the “public interest, which is always on the side of liberty, can be invoked to justify the non-enforcement of a restraint.”¹¹¹ All interference with the individual liberty to trade was regarded as against public policy and therefore void.¹¹² This was the position in South Africa until the decision in *Magna Alloys* replaced the value placed on the liberty to earn a living for sanctity of contract as discussed above.

In South African case law the freedom to work as a component of human dignity has been described as follows in *Minister of Home Affairs v Watchenuka*:¹¹³

“The freedom to engage in productive work – even where that is not required in order to survive – is indeed an important component of human dignity ... for mankind is pre-eminently a social species with an instinct for meaningful association. Self-esteem and the sense of self-worth – the fulfilment of what it is to be human – is most often bound up with being accepted as socially useful.”¹¹⁴

In *Affordable Medicines Trust v Minister of Health*¹¹⁵ the court stated that

“[w]hat is at stake is more than one’s right to earn a living, important though that is. Freedom to choose a vocation is intrinsic to the nature of a society based on human dignity as contemplated by the Constitution. One’s work is part of one’s identity and is constitutive of one’s dignity. Every individual has a right to take up any activity which he or she believes himself or herself prepared to undertake as a profession and to make that activity the very basis of his or her life. And there is a relationship

¹⁰⁷ Sutherland *Restraint of Trade Doctrine* 51-52

¹⁰⁸ Du Plessis & Davis (1984) *SALJ* 97

¹⁰⁹ *Barkhuizen v Napier* 2007 7 BCLR 691 (CC) para 152

¹¹⁰ Sutherland *Restraint of Trade Doctrine* 31

¹¹¹ Lord Shaw of Dunfermline in *Mason v Provident Clothing and Supply Company Limited* [1913] AC 724

¹¹² Lord McNaghten in *Nordenfelt v The Maxim Nordenfelt Guns and Ammunition Co Ltd* [1894] AC 565

¹¹³ 2004 2 BCLR 120 (SCA)

¹¹⁴ Para 27

¹¹⁵ 2005 6 BCLR 529 (CC)

between work and the human personality as a whole. It is a relationship that shapes and completes the individual over a lifetime of devoted activity; it is the foundation of a person's existence."¹¹⁶

The freedom to work is therefore an important human right as it is a means to maintain dignity and self-respect¹¹⁷ by providing for one's own and one's family's upkeep; not to be dependent on anyone or the state; to take part in activities of society regarded to be to the benefit of society and thereby earn the respect of society;¹¹⁸ to express oneself and to develop the self.¹¹⁹

On the other hand, if a person is not able to work, this will lead to social exclusion¹²⁰ because of poverty and the lack of social interaction inherent in a workplace. The person and their family would also most likely become dependent on the state or the community.

Section 22 of the Constitution, which protects the right to work, the importance of which is spelled out above, should furthermore not be interpreted in isolation. The rights to dignity (section 10), freedom of movement (section 21), the right not to be subjected to forced labour (section 13), freedom of association (section 18), and the right to fair labour practices (section 23) should also be taken into consideration when the content of the right to freely choose a trade, occupation or profession is considered.

10 The inequality of the bargaining positions of parties

English courts have held that even if the contract was freely entered into, there is a difference between a restraint agreement in an employment contract and a restraint agreement in a contract for the sale of a business. Lord MacNaghten stated in the *Nordenfelt* case that

"there is obviously more freedom of contract between buyer and seller than between master and servant or between an employer and a person seeking employment."¹²¹

Lord Shaw of Dunfermline agreed with this statement in *Mason v Provident Clothing* and stated that in his opinion

"there is much greater room for allowing, as between buyer and seller, a larger scope for freedom of contract and a correspondingly large restraint in freedom of trade, than there is for allowing a restraint of the opportunity for labour in a contract between master and servant or an employer and an applicant for work."¹²²

Regard for the unequal bargaining position of parties in employment contracts forms the basis for the disfavour with which covenants in restraint of trade are treated in many states in the USA.¹²³ In a few states, notably

¹¹⁶ *Affordable Medicines Trust v Minister of Health* 2005 6 BCLR 529 (CC) para 59

¹¹⁷ A van Niekerk, M Christianson, M McGregor, N Smit & S van Eck *Law @ Work* (2008) 3

¹¹⁸ *Minister of Home Affairs v Watchenuka* 2004 2 BCLR 120 (SCA) paras 26-27

¹¹⁹ *Affordable Medicines Trust v Minister of Health* 2005 6 BCLR 529 (CC) para 59

¹²⁰ H Collins, KD Ewing & A McColgan *Labour Law Text and Materials* (2005) 5

¹²¹ *Nordenfelt v The Maxim Nordenfelt Guns and Ammunition Co Ltd* [1894] AC 565

¹²² *Mason v Provident Clothing and Supply Company Limited* [1913] AC 738

¹²³ *National Motor Club of La., Inc. v. Conque*, 173 So. 2d 238, 241 (La. Ct. App. 3d Cir. 1965) (Louisiana); *Omniplex World Servs. Corp. v. US. Investigations Servs. Inc.*, 618 S.E. 2d 340, 342 (Virginia); J Boatman "Contract Law: As clear as Mud: The Demise of the Covenant not to compete in Oklahoma" (2002) 55 *Okla. L. Rev.* 491-506

California, this type of covenant is prohibited.¹²⁴ In states where restraint agreements are not prohibited, the courts have taken a wide range of factors into consideration in establishing the reasonableness of the restraint.¹²⁵

In *Afrox Healthcare BP (Cape) v Strydom*¹²⁶ the South African Supreme Court of Appeal held that inequality of bargaining power is a factor that would be taken into consideration by courts in establishing the public interest.¹²⁷ In *Barkhuizen v Napier* Ngcobo J agreed with the principle that inequality of bargaining positions would have an influence on the enforceability of a contract and added that the constitutional values of equality and dignity may prove decisive.¹²⁸

In *Napier v Barkhuizen*¹²⁹ the Supreme Court of Appeal was willing to take the relative bargaining positions of the parties in an insurance contract into account in determining whether the contract was against public policy, but could not do so in the absence of evidence before the court:

"In the present case, the evidence is so scant that we can only speculate on the plaintiff's bargaining position in relation to the insurer. This is because there was no evidence regarding the market in short-term insurance products; whether a variety of such products is available; the number of suppliers, and their relative market share; whether all or most short-term insurers impose a time-bar; whether a diversity of time-limits is available to those seeking short-term insurance cover, and over what range they fall... All this would bear on the critical question, which is whether the plaintiff in effect was forced to contract with the insurer on terms that infringed his constitutional rights to dignity and equality in a way that requires this court to develop the common law of contract so as to invalidate the term. But without any inkling regarding the issues set out above, the broader constitutional challenge cannot even get off the ground."¹³⁰

The factors enumerated by the court are quoted in full to illustrate the factual detail that could play a role in indicating that parties are not in an equal bargaining position in the insurance context. By analogy to the above, factors that should be taken into account to establish whether a restraint agreement was voluntarily entered into are the following:

- the experience and skills or lack of experience and skills of the employee;
- the demand in the labour market for the employee's skills;
- whether there is a high rate of unemployment;
- the state of the economy and the unemployment rate;
- personal circumstances such as family responsibilities that would place pressure on an employee in finding a job in a certain area; and
- the age of the employee (young people and people above 50 may find it more difficult to find employment).

¹²⁴ K O'Neill "Should I stay or should I go? – Covenants not to compete in a Down Economy: A Proposal for Better Advocacy and Better Judicial Opinions" (2010) 6 *Hastings Bus LJ* 83 102

¹²⁵ In Nebraska in the USA the courts have taken into account factors such as the employee's training, health, education, and needs of his family; the current conditions of employment; and the necessity of the employee changing his profession or residence in establishing the reasonableness of the restraint *Philip G. Johnson & Co. v. Salmen*, 1982 211 Neb 123, 317 NW 2d 900, 904

¹²⁶ 2002 6 SA 21 (SCA)

¹²⁷ 131

¹²⁸ *Barkhuizen v Napier* 2007 7 BCLR 691 (CC) para 59

¹²⁹ 2006 4 SA 1 (SCA)

¹³⁰ *Napier v Barkhuizen* 2006 4 SA 1 (SCA) paras 15-16 (emphasis added)

The above factors could conveniently be grouped together under the concept of “economic dependence”, which was recently pointed out as one of the most important factors indicating that a person is an employee and not an independent contractor.¹³¹ The concept of economic dependence could also be used in the present context to indicate that an employee was economically dependent on the employer to such an extent that there was no real bargaining power and that there was therefore no choice for the employee but to agree to the particular restraint.

The concerns raised by Sachs J in *Barkhuizen v Napier*¹³² in regard to questions about real consensus in standard form contracts should also be taken into consideration. Often agreements in restraint of trade are drawn up by in-house lawyers, as an addendum to all employment contracts and not as a specific clause for a specific employee.¹³³ The standard restraint agreement with many sub-clauses and legal jargon has to be signed by all employees, regardless of their position in the firm. The inequality in bargaining power and the absence of freedom of contract in such a situation is obvious.

The unequal bargaining position of employees was often denied by South African courts in pre-constitutional times,¹³⁴ but also by courts delivering judgments after the advent of the Constitution.¹³⁵ In these judgments it has been held that restraint agreements in employment contracts do not warrant any special treatment. Didcott J in *Roffey v Catterall, Edwards & Goudré* stated as follows:

“Economic development, industrial legislation, trade unionism, and other modern phenomena have so strengthened large categories of employees that their negotiating force is often equivalent or superior to that of their employers.”¹³⁶

Wallis J in *Den Braven*, criticising Davis J’s judgment in *Advtech v Kuhn* that restraints of trade in employment contracts should be regarded in a different light after the advent of the Constitution, stated that:

“There appears to be a view that restraint of trade agreements justify special and separate treatment within our law of contract and that the existing state of our law requires reconsideration. The further impression left by all this is that there is in principle an objection to such agreements. If that is a correct reasoning on both grounds I am unable to share the learned judge’s view. The importance of the decision in *Magna Alloys* is that it removed restraint of trade agreements from being a special and isolated type of contract looked upon with particular approbation by the courts and placed them squarely within the mainstream of the law of contract as agreements concluded and enforceable in the ordinary course, but unenforceable where their enforcement would be in conflict with public policy”.¹³⁷

This view of Wallis J may be appropriate in respect of restraint agreements concluded outside the employment context, but it is not appropriate for agreements concluded as part of an employment contract. The basis for labour law as a separate discipline is the acknowledgement of the fact that the

¹³¹ *State Information Technology Agency (Pty) Ltd v Commission for Conciliation, Mediation & Arbitration* 2008 29 ILJ 2234 (LAC) para 12

¹³² *Barkhuizen v Napier* 2007 7 BCLR 691 (CC) paras 123-175

¹³³ *Den Braven Ltd v Pillay* 2008 6 SA 229 (D) para 30

¹³⁴ *Roffey v Catterall, Edwards and Goudré (Pty) Ltd* 1977 4 All SA 482 (N) 487

¹³⁵ *Knox D’Arcy v Shaw* 1996 2 SA 651 (W) 659; *Den Braven Ltd v Pillay* 2008 6 SA 229 (D) para 27

¹³⁶ *Roffey v Catterall, Edwards & Goudré (Pty) Ltd* 1977 4 All SA 482 (N) 487

¹³⁷ *Den Braven Ltd v Pillay* 2008 6 SA 229 (D) para 35

employees are in a subordinate position because of their inferior bargaining position.¹³⁸ For this reason legislation establishes minimum conditions of work and regulates collective bargaining. By these measures labour legislation endeavours to place employers and employees in an equal bargaining position. Some employees may be in an equal bargaining position to their prospective employer at the conclusion of the contract, but highly skilled employees are the exception, especially in South Africa, where unemployment rates are well over 25%.¹³⁹ Highly skilled employees will often receive some benefit (excluding simply being employed) as *quid pro quo* for agreeing to a restraint. If there is no *quid pro quo* (as is the usual position), this may be an indication of an unequal bargaining position.

Should the superior courts not develop the common law to take the unequal bargaining position of employees into account to give effect to the Constitution and in so doing protect employees, the legislator could solve the problem as was done in Germany.

11 The regulation of restraint clauses by legislation in Germany

Restraint clauses in Germany are in general not regarded as invalid, because of the principle of liberty to contract, which is protected in Article 2¹⁴⁰ of the German *Grundgesetz* (Basic Law or Constitution). However, restraint clauses in employment contracts are strictly regulated by legislation in §§ 74-75f of the *Handelsgesetzbuch* (HGB) read with § 110 of the *Gewerbeordnung* (GWO). Restraint clauses have to comply with the following requirements to be enforceable:

- the employer must have a protectable interest;¹⁴¹
- the clause must be in writing;¹⁴²
- the duration of all restraints is limited to two years after the termination of the employment contract;¹⁴³
- the employer has to pay half of the employee's salary for each year that the restraint operates (*bezahlte Karenzeit*);¹⁴⁴ and
- the courts will not enforce a restraint that causes unreasonable disadvantages for the employee in terms of the duration, geographical area and subject of competition.¹⁴⁵

¹³⁸ "[T]he relation between an employer and isolated employee or worker is typically a relation between a bearer of power and one who is not a bearer of power. In its inception it is an act of submission, in its operation it is a condition of subordination, however much the submission and the subordination may be concealed by that indispensable figment of the legal mind known as the 'contract of employment'. The main object of labour law has always been, and we venture to say will always be, to be a countervailing force to counteract the inequality of bargaining power which is inherent and must be inherent in the employment relationship" (PL Davies & M Freedland *Kahn-Freund's Labour and the Law* 3 ed (1983) 18)

¹³⁹ Statistics South Africa *Quarterly Labour Force Survey* (04-05-2010) 1 (January-March)

¹⁴⁰ Article 2 makes provision for "personal freedoms"

¹⁴¹ § 74 a I 1 HGB

¹⁴² § 74 I 1 HGB

¹⁴³ § 74 a I 3 HGB

¹⁴⁴ § 74 I 1 HGB

¹⁴⁵ M Weiss & M Schmidt "Germany" in R Blanpain (ed) *International Encyclopaedia for Labour Law and Industrial Relations* 7 (RS 2010) para 337

In the event of the court finding that the restraint is unenforceable because the agreement did not comply with the requirements set out above (for example a non-protectable interest), the employee still has the choice to adhere to the agreement and to be paid the agreed amount.¹⁴⁶ If this is the employee's choice, such employee is then obliged to refrain from taking up employment as specified in the restraint clause. The former employer is entitled to information about the new employer of its erstwhile employee, the scope of its business and the duties of the employee.¹⁴⁷

Although the German *Grundgesetz* protects the right to freely choose an occupation in Article 12, the German courts do not have to rely on the *Grundgesetz* to ensure fairness, as the German legislator has given effect to the constitutional right to freely choose an occupation as discussed above. These rules ensure balance in a relationship which is often skewed as a result of the unequal bargaining positions of employers and employees.

Some of the requirements for valid restraint clauses in Germany are similar to the requirements for reasonableness *inter partes* in South African law. For instance, the employer must have a protectable interest and the restraint must not be unreasonable in regard to duration and geographical area. Payment of all employees (and not only highly skilled employees) will ensure that the employer does not lightly insist on a restraint. If the employer is required to pay 50% of the normal remuneration of the employee, this would seem to be fair to both the employer and employee. The employer is further protected in that the employee has to provide information on a new employer.

The above regulation of employment restraints in the German system could also be taken into account in developing the South African common law. In terms of section 39(1)(c) of the final Constitution, courts may consider foreign law when interpreting the Bill of Rights. When interpreting sections 22 and 23 of the Constitution in the context of employment restraints, the measures taken by the German legislator could be considered as an example of how to ensure a more balanced relationship.

12 Conclusion

After the advent of the Constitution several judgments of the High Court favoured a new approach to restraint of trade clauses in employment contracts. In these judgments it was held that the Constitution, and especially section 22 of the Constitution, has the effect that the common law position in terms of which the maxim *pacta sunt servanda* enjoys preference to freedom to trade has now been changed. According to these judgments, the burden to prove reasonableness of the restraint should in the light of the Constitution now rest on the employer.¹⁴⁸ Conflicting judgments held that the common law position

¹⁴⁶ Decision of the Bundesarbeitsgericht (BAG) 28 6 2006, AZR,407/25

¹⁴⁷ BAG 22 4 1967, BGB §242 This paragraph deals with *Treu und Glauben* (performance in good faith) and provides as follows: "An obligor has a duty to perform according to the requirements of good faith, taking customary practice into consideration"

¹⁴⁸ *Advtech Resourcing Ltd t/a Communicate Personnel Group v Kuhn* 2008 2 SA 375 (C) para 28; *Coetzee v Comitis* 2001 1 All SA 538 (C) para 40

(as set out in *Magna Alloys*) is not in conflict with the Constitution and that the onus should therefore remain on the employee.¹⁴⁹

The fact that the relationship between employee and employer is increasingly being regulated by legislation,¹⁵⁰ is an acknowledgement of the fact that common law lawfulness alone is not sufficient to regulate the employment relationship. The contract of employment has at least since 1944 been regarded as a special kind of contract in terms of which man does not sell a commodity, but sells himself.¹⁵¹ The common law contract of employment still forms the basis of the employment relationship, but the freedom of contract of parties is limited to protect employees.

However, clauses in restraint of trade in employment contracts still lag behind in respect of protection afforded to employees. There is no legislation regulating these agreements and the unequal bargaining position of employees has not been taken sufficiently into consideration in judgments establishing the reasonableness of the restraint. Therefore, freedom to contract, which in some judgments is read into the constitutional right to dignity, still enjoys preference when balanced against freedom of trade. The rules of the common law, now generally regarded as inadequate to regulate the employment relationship, are left intact to regulate without interference a very important part of the employment contract.

In the light of the constitutional right to dignity, freedom of association, freedom of forced labour, freedom of movement, freedom to choose a trade and the right to fair labour practices, which could all be potentially limited by a restraint, the common law rules regulating restraint agreements in employment contracts should be amended to reflect these values.

To attain this, the courts could develop the common law applicable to restraint agreements in terms of section 8(3) of the Constitution.¹⁵² This would entail testing the common law rules pertaining to reasonableness of the restraint directly against section 22 and the other relevant rights in the Constitution.

Alternatively, in the light of the criticism of the Constitutional Court in *Barkhuizen v Napier* against this approach, the courts could develop the common law through the prism of public policy in terms of section 39(2) to reflect the values of the Constitution without directly testing the law of contract against a specific constitutional right. Should courts develop the common law test for reasonableness in terms of section 39(2), freedom to trade should – in the light of the value of freedom to work and the unequal bargaining position of employees – enjoy primacy instead of *pacta sunt servanda*. The effect of developing the common law either through section 39(2) or section 8(3) would then be that the onus to prove that the restraint is reasonable would shift from the employee to the employer.

¹⁴⁹ *Den Braven Ltd v Pillay* 2008 6 SA 229 (D) para 35

¹⁵⁰ Basic Conditions of Employment Act 75 of 1997; Labour Relations Act 66 of 1995

¹⁵¹ International Labour Organisation (ILO) *ILO Declaration of Philadelphia* (1944) <http://www.ilocarib.org/tt/projects/cariblex/conventions_23.shtml> (accessed 06-05-2010)

¹⁵² *Davis J in Advtech Resourcing Ltd t/a Communicate Personnel Group v Kuhn* 2008 2 SA 375 (C) para 30, stated that both ss 8 and 39(2) could be conducive to revisiting the issue of restraint of trade

Should the courts not give effect to section 22 and other constitutional rights impacting on restraint agreements, the legislator could alternatively bring relief. The German example could be a model for reform in South Africa and could add much needed protection to employees who are locked into unreasonable restraints, or employees who have to conclude unreasonable restraint agreements in order to secure employment.

SUMMARY

Clauses in restraint of trade in employment contracts still lag behind in respect of protection afforded to employees. There is no legislation regulating these agreements and the unequal bargaining position of employees has not been taken sufficiently into consideration in judgments establishing the reasonableness of the restraint. The rules of the common law, now generally regarded as inadequate to regulate the employment relationship, are left intact to regulate without interference a very important part of the employment contract.

In the light of the constitutional right to dignity, freedom to choose a trade and the right to fair labour practices, which could all be potentially limited by a restraint, the common law rules regulating restraint agreements in employment contracts should be amended to reflect these values.

To attain this, the courts could develop the common law applicable to restraint agreements in terms of section 8(3) of the Constitution. This would entail testing the common law rules pertaining to reasonableness of the restraint directly against section 22 of the Constitution.

Alternatively, in the light of the criticism of the Constitutional Court in *Barkhuizen v Napier* against this approach, the courts could develop the common law through the prism of public policy in terms of section 39(2) to reflect the values of the Constitution without directly testing the law of contract against a specific constitutional right. Should courts develop the common law test for reasonableness in terms of section 39(2), freedom to trade should – in the light of the value of freedom to work and the unequal bargaining position of employees – enjoy primacy instead of *pacta sunt servanda*. The effect of developing the common law would then be that the onus to prove that the restraint is reasonable would shift from the employee to the employer.